LIMITED SCOPE AUDIT REPORT

ON SELECTED NATIONAL ENDOWMENT FOR THE ARTS GRANTS TO THE

COMMONWEALTH COUNCIL FOR ARTS AND CULTURE

REPORT NO. LS-10-02

August 17, 2010

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INTRODUCTION

BACKGROUND

The Commonwealth Council for Arts and Culture (Council), a division under the umbrella of the Department of Community and Cultural Affairs is the sole arts agency in the Commonwealth of the Northern Mariana Islands (CNMI) that provides and fosters programs, projects and opportunities with the emphasis on culture, traditions and education through arts. The Council was created in 1980, by law, to serve as an agency to preserve, protect and promote the traditions and cultures important to the identity of the CNMI.

OBJECTIVE AND SCOPE

The objectives of this limited scope audit were to determine whether:

- The grantee fulfilled the financial and compliance requirements as set forth in the grant awards;
- The total project costs claimed under the grants were reasonable, allocable and allowable;
- The required match was met on National Endowment for the Arts (NEA) grant funds; and
- The objectives for which the grants were awarded were actually accomplished.

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. The "Standards" require that we obtain sufficient, competent, and relevant evidence to afford a reasonable basis for our findings and conclusions.

During the period under review, the Council had five NEA grants active with awards totaling \$1,012,020 (see Appendix A), including one grant funded by the American Recovery and Reinvestment Act of 2009. However, our audit was limited to those four grants in which NEA funds had been drawn down and costs had been reported.

 Grant Number
 05-6100-2053

 Grant Number
 06-6100-2043

 Grant Number
 07-6100-2069

 Grant Number
 08-6100-2056

Grant Number 09-6188-2128 (not reviewed)

PRIOR AUDIT COVERAGE

During the past five years, the NEA Office of Inspector General had not issued any audit reports on Federal grants awarded to the Council. However, the Council was included in the CNMI's Office of Management and Budget (OMB) Circular A-133 audit for the year ended September 30, 2008. The auditors, Deloitte & Touche, LLC, issued a qualified opinion.

Although the auditors did not specifically question any costs under the NEA grants, their "Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133," noted 57 reportable conditions relating to compliance and internal controls, 40 of which were considered significant deficiencies and 11 were considered material weaknesses.

Some of these conditions which may impact NEA's funding were noncompliance with requirements regarding allowable costs/cost principles and activities, cash management, equipment management, prohibitions concerning awards to excluded parties, procurement and reporting requirements, and matching level of effort and eligibility requirements.

RESULTS OF AUDIT

Overall, our audit concluded that the Council should strengthen its policies and procedures and implement corrective actions to improve its management of Federal funds. Specifically, we found that the Council did not:

- Have a system in place that adequately tracks all costs reported.
- Maintain appropriate expense documentation and may have inappropriately awarded grants to ineligible organizations and individuals.
- Maintain the required personnel activity reports.
- Have adequate internal controls in place
- Have a Section 504¹ self-evaluation on file.

The General Terms, Sections 15 and 16, the Guide and applicable OMB Circulars states in part:

Recipients must have accounting structures that provide accurate and complete information about all financial transactions related to each Federally-supported project.

The grantee must maintain financial records, supporting documentation (such as cancelled checks, invoices, contracts, travel reports, donor letters, in-kind contribution reports, and personnel activity reports), statistical records, and all other records pertinent to an award according to the provisions outlined in OMB Circular A-110, Section 53 or the "Common Rule," OMB Circular A-102 Section 42, as applicable.

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¹ Section 504 Rehabilitation Act of 1973.

FINANCIAL MANAGEMENT SYSTEM

The NEA's General Terms and Conditions for Grants and Cooperative Agreements to Organizations (General Terms) which has financial management requirements or refers to the Office of Inspector General's Financial Management Guide for State & Local Governments (Guide), is provided to each applicable grantee. Financial management requirements are also provided in OMB Circulars A-102, Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments, A-87 (2 CFR 225), Cost Principles for State, Local, and Indian Tribal Governments and A-133, Audits of States, Local Governments, and Non-Profit Organizations.

The Council did not have a financial management system in place to adequately track, monitor and report accurate and complete costs. Based upon the preliminary findings of this audit, the NEA suspended its funding to the Council in October 2009. NEA *General Terms*, *Section* 29(a) states in part:

That funding may be suspended to quickly protect the interest of the government when NEA receives information that indicates a lack of business integrity or business honesty and/or any other cause of so serious or compelling a nature that it affects an organization's present responsibility while the specifics are investigated. A suspension may result in debarment from receiving Federal funding government-wide for up to three years.

Our review found the following deficiencies in the Council's financial management system:

UNALLOWABLE EXPENSES

Mismanagement and Potential Conflict of Interest

Indicators of mismanagement and conflict of interest were identified in each of the grants we reviewed. The Council awarded grants to ineligible recipients and organizations such as former and current government and Council employees as well as Board members. We also found that grants were awarded to an employee who neither applied nor received award funds. Additionally, expenses were also charged for travel, per diems and stipends for ineligible recipients.

Mismanagement

During our review of the expenditure listings for grants below, we noted several grants were awarded to an employee, in the amount of \$18,350, charged to both the NEA grant and matching portions. However, the employee stated that they did not apply nor receive any of these awards, with the exception of a grant in the amount of \$300.00 for teaching traditional coconut weaving. We also reviewed a copy of an award check made payable to the same employee, addressed to the employee at the Council's P.O. Box, however it was picked up by someone other than the employee. Therefore, we are recommending that NEA disallow the following costs charged to the grants, reducing the total outlays reported by the indicated amounts for each grant:

Grant Number	<u>Amount</u>
05-6100-2053	\$ 11,250
06-6100-2043	\$ 7,100 \$ 19,250
Total	<u>\$ 18,350</u>

We recommend the Council develop written policies and implement procedures to establish <u>code</u> of <u>conduct</u> and <u>conflict of interest standards</u> in accordance with the CNMI's <u>Department of Finance Division of Procurement and Supply – CNMI Procurement Regulations</u>, NEA General Terms and consistent with OMB Circular A-102, Subpart C, Section 36.

Potential Conflict of Interest

For the grants below, we found the Council made several awards and payments to ineligible award recipients and companies such as former and current employees, employees of the CNMI Office of the Governor, relatives, Council Board members and companies owned by relatives.

NEA *General Terms*, Section 30, clearly states that subrecipients should not be employees or affiliated with the prime recipient. The Council's guidelines also prohibit awarding funds which could create actual or the appearance of a conflict of interest. CNMI's *Department of Finance Division of Procurement and Supply – CNMI Procurement Regulations*, para. 70-30.3-720 and 70-30.3-740, "Employee Conflict of Interest" states in part:

- It is a breach of ethical standards for any employee (former or present) to participate directly or indirectly in the procurement process, where the employees participates in the approval process and knows that a member of the employee's immediate family has a financial interest.
- Public official or employees may not participate in transactions that they may substantially influence if they know that a relative, friend, or associate has a substantial financial interest in them.

As a result, we are recommending that NEA disallow the following costs charged to the grants, reducing the total outlays reported by the indicated amounts for each grant:

Grant Number	Amount
05-6100-2053	\$20,700
06-6100-2043	\$23,801
07-6100-2069	\$16,675
08-6100-2056	\$ 3,200
Total	<u>\$64,376</u>

Capital Expenditures and Food

For each of the grants audited, the Council claimed costs that were unallowable under OMB Circular A-102 and A-87, NEA guidelines and/or CNMI Procurement Regulations. For example, we found instances of capital expenditures which were not preapproved, as required by NEA and OMB. The Council also charged costs for food expenses for employees of the Council and extended hotel costs for participants of the Flame Tree Arts Festival.

Capital Equipment

The Council purchased two vehicles with NEA funds without *prior* written approval from the NEA, as required by NEA *General Terms*, Section 19 and OMB Circular A-87, Attachment B, Section 19(3) c. When questioned about the purchase, the Council's staff informed us that the vehicles were included in the budget. However, both project budgets refer to "maintenance of vehicles." Therefore, we are recommending that NEA disallow costs for the two vehicles charged to the grants, reducing the total outlays by the indicated amounts for each grant:

Grant Number	Amount
07-6100-2069	\$17,695
08-6100-2056	\$22,895 \$40,500
Total	<u>\$40,590</u>

We recommend that the Council develop written policies and implement procedures to ensure that only actual and allowable costs are reported on its payment requests and the final Federal Financial Report (FFR)². Those procedures should ensure that employees, who prepare the payment requests FFRs, are familiar with the cost principles of OMB Circulars A-102 and A-87.

We also recommend that the Council develop written policies and implement procedures to ensure that any capital equipment, purchased with Federal funding, is included in its project budget and approved by NEA prior to purchase.

Food and Entertainment

The Council charged expenditures for food and extended hotel stays to the grants below. Food was provided to the public, participants and Council *employees*. In one instance, food was provided to staff while being paid overtime for their participation in program activities. The Council also included costs for extended hotel stays for delegates who attended the Flame Tree Arts Festival. However, we could not determine the purpose or dates of the extended stays from the supporting documentation provided.

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² Formerly the Financial Status Report (FSR).

Under OMB Circular A-87, costs for entertainment³ or costs not reasonable to the project⁴ are unallowable. Therefore, we are recommending that the NEA disallow the following costs, reducing the total outlays reported by the indicated amounts for each grant:

Grant Number	Amount
05-6100-2053 06-6100-2043	\$ 5,120 \$ <u>12,613</u>
Total	<u>\$ 17,733</u>

QUESTIONED COSTS

Personnel Activity Reports

The Council did not maintain personnel activity (time and effort) reports for all employees whose salaries and fringe benefits are charged, in whole or in part, to either the *award* or the *matching funds* for all of the grants audited. At the time of the awards, personnel activity reports were required for all grant awards of \$50,000 or more and each of the Council awards we reviewed exceeded \$50,000. The requirement for personnel activity reports is mandated by OMB and is detailed in the NEA *General Terms*, Section 18. A sample personnel activity report is also provided in the *General Terms*, which states in part:

You must maintain personnel activity ("Time & Effort") reports for any employee whose salary is charged, in whole or in part, to either the award or the matching funds if:

- your award is \$50,000 or greater, or
- you are on an alternative method of funding (as noted in an award document or the Inspector General's audit follow up report).

During the site visit, the Council staff informed us that only the Executive Director's salary is charged to the NEA grant; however, during our review we found that all of the employees' salaries were included in the total outlays reported.

Amount
\$205,051
\$149,408
\$179,855
\$ 40,393
<u>\$574,707</u>

As a result of not maintaining personnel activity reports, we are questioning the salary and fringe benefits costs, included in the total outlays, in the amount of \$574,707. The Council should

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³ Office of Management and Budget (OMB), Circular A-87 as amended, *Cost Principles for State, Local, and Indian Tribal Governments*, Attachment B, Section 18, Entertainment Costs.

⁴ OMB Cir. A-87, Attachment A, Section. C.2, Reasonable Costs.

submit personnel activity reports to the OIG to support questioned salaries. Without the additional documentation, a potential refund may be due to the NEA.

We recommend that the Council provide additional documentation to support salaries and fringe benefits costs charged to the grant. We also recommend that the Council develop written policies and implement procedures to ensure that personnel activity (time and effort) reports are maintained for any employee whose salary is charged, in whole or in part to future grant awards of \$50,000 or more. Personnel activity reports must (1) reflect an after-the-fact distribution of the actual activity of each employee, (2) be prepared at least monthly and must coincide with one or more pay periods and (3) must be signed by the employee.

Travel Expenses

For each of the grants audited, the Council claimed costs for travel which may be unallowable under OMB Circular A-87, Attachment B, Section 41.

The Council charged travel, stipends and per diem expenses to the grants below for several ineligible recipients such as, employees from other CNMI government agencies and relatives of Council Board members. OMB Circular A-87, states in part, that travel costs are allowable for expenses for transportation, lodging, subsistence, and related items incurred by *employees traveling on official business*. Therefore, we are questioning the following travel costs charged to the grants:

Grant Number	<u>Amount</u>
05-6100-2053	\$ 2,496
06-6100-2043	0^5
07-6100-2069	\$46,175
08-6100-2056	\$30,080
Total	\$78,751

We recommend the Council develop written policies and implement procedures to ensure that only allowable travel expenses are charged to the grant and matching costs for eligible individuals, in accordance with OMB Circular A-87.

INTERNAL CONTROLS

We identified internal control weaknesses regarding documentation, subrecipient monitoring, policies for grant management, controls over assets, spending authority and matching expenditures.

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⁵ Costs included under "Conflict of Interest" Section.

Inadequate Documentation

The Council did not submit accurate and complete reports and/or payment request documents. In most cases, the Council had to resubmit reports and/or requests for payments due to math errors, duplicate requests, incomplete documentation and unallowable costs. In some cases, administrative actions such as withholding payments and de-obligating funds were used to resolve reporting issues. For all of the grants audited, the Council requested extensions for final report submissions. In addition, for Grant Numbers 07-6100-2069, 06-6100-2043 and 05-6100-2053, extensions were requested to allow time to expend funds that had not been committed by the end of the original support period.

The Council's inability to report costs accurately and timely has caused excessive use of the Grants and Contracts Office available resources to process payments. Recipients of federal funding are mandated by OMB to have adequate accounting structures which would provide accurate and complete information.

We recommend that the Council develop written policies and implement procedures to track, monitor and report accurate and complete information for all financial transactions (reports/payment requests) related to NEA grants. Procedures for an independent review of reports/requests, prior to submission to the NEA should be included. This is to ensure that only costs which are reasonable, allowable and allocable in accordance NEA and OMB guidelines are reported. Those procedures should direct employees, who prepare the FFRs and/or payment requests, become familiar with the costs principles of applicable OMB Circulars. The Council should also develop and implement required written procedures to ensure that all NEA funds are committed/obligated before the end of the award period.

Subrecipient Monitoring

The NEA grantee is responsible for ensuring that subrecipients expend their awards in accordance with the laws, regulations, and provisions of the underlying grant. However, we found that the Council did not adequately monitor subrecipients. For example, the Council did not provide subrecipients with identification information such as the Catalogue of Federal Domestic Assistance title or number in accordance with OMB Circular A-133, Subpart D. The Council also did not provide information to subrecipients regarding Federal requirements for managing Federal funds or evidence that funding was provided by NEA.

The Council did not have procedures (such as submitting Single Audit reports) in place to monitor subrecipients in accordance with OMB Circular A-133, Subpart D. According to the Council staff, no awards had been made to grantees which would require OMB Circular A-133 reviews. However, the Council, as a pass-through entity, is required to ensure that subrecipients, who expend more than \$500,000 in federal funding in any fiscal year, have met the OMB Circular A-133 requirements for that fiscal year.

The Council also did not adequately maintain subrecipients' documentation. Some files lacked pertinent documentation such as final reports and budget data as required by NEA *General Terms* and Council's guidelines. The Council's guidelines require all reports from prior awards

to the recipient, be submitted <u>before</u> receiving another award. Without final reports, there is no documented evidence to support that projects were completed in accordance with the Council's award provisions. Grants were also awarded to subrecipients who did not submit the required budget as part of their application. According to Council guidelines, applicants <u>must</u> provide a project budget with the application. The guidelines also stated that applications that are missing any of the required items, including the project budget, *will be not reviewed*. We also found that payments were made to artists without any documentation between the artists and Council. Without some type of agreement or contract between the Council and the artists, there is no evidence of an agreement for requested services and/or products. According to NEA *General Terms*, Section 30:

The Federal laws, rules, regulations and OMB Circulars that apply to Arts Endowment organizational award recipients generally also apply to such organizations when they receive a subgrant through an Arts Endowment-supported award. Subgrant agreements must include a requirement that the subgrantee provides final reports and any other information or reports necessary for you to fulfill all applicable Federal reporting requirements. Records pertinent to the award are to be maintained for three years following submission of the final report.

OMB A-133 also states in part:

Pass-through entities should ensure that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.

We recommend the Council develop written policies and implement procedures to monitor subrecipients in accordance with the NEA *General Terms* and OMB Circular A-133. The policies and procedures should also ensure that subrecipients' documentation is complete and maintained for a period of three years from the date of its Final Financial Report⁶ submission to the NEA.

Grant Management Policies

We found that while the Council followed the CNMI's "Department of Finance Division of Procurement and Supply – CNMI Procurement Regulations," it lacked a written document in the form of a manual or handbook on Federal grant policies, procedures, and requirements. We also found that some of the staff was not familiar with several requirements of the NEA *General Terms* and OMB guidance. OMB Circular A-110 states in part:

Recipients of Federal awards should have written procedures for determining the reasonableness, allocability and allowability of costs in accordance with the provisions of the applicable Federal cost principles and the terms and conditions of the award.

⁶ Formerly Financial Status Report (FSR).

The Council's could further enhance their knowledge and avoid potential systematic problems if the Council developed a written grants manual or handbook. The handbook should contain policies and procedures relating specifically to managing Federal grants and publications such as the NEA *General Terms*, the *Financial Management Guide for State & Local Governments*, applicable *OMB Circulars* and other publications on Federal requirements. It should also include guidance on financial and grant management, internal controls and determining allowable and allocable costs.

We recommend that the Council develop a manual/handbook, which contains policies and procedures relating specifically to managing Federal grants.

Controls Over Assets

Vehicles and Cell Phones

At the time of our review, the Council did not have any controls in place to account for and maintain vehicles or cell phones acquired with Federal funds. All vehicles and cell phone expenditures were charged directly to a grant. There were no written policies and procedures for vehicles or cell phone accountability, such as inventory listings, assignment or monitoring of vehicle usage. The Council also did not have procedures to ensure that all drivers of government vehicles were, in fact, licensed drivers. We were also informed by the Council staff that vehicles were taken home regularly and used for both Council and personal use. OMB Circular A-102, Subpart C Section 32 states in part:

Recipients' property management standards for equipment acquired with Federal funds and Federally-owned equipment shall include equipment records maintained accurately and that a control system shall be in effect to insure adequate safeguards to prevent loss, damage, or theft of the equipment. It further states that a physical inventory of equipment shall be taken and the results reconciled with the equipment records at least once every two years. The recipient shall, in connection with the inventory, verify the existence, current utilization, and continued need for the equipment.

We recommend the Council develop written policies and implement procedures to ensure adequate control over all assets acquired with Federal funds.

Documenting Matching Expenditures

The Council did not adequately identify costs for matching expenditures charged to the grant. During our site visit, the Council provided two expenditure listings to support the total outlays reported on the Financial Status Reports (FSRs). We were informed by the staff that the expenditures up to the amount of the grant award were maintained in the CNMI financial system. However, the matching portion was maintained at the Council. Details of the expenditure listings provided for each of the grants are detailed below:

	Adjusted	Total		
	Total Outlays	Expenditures	NEA Grant	Council Matching
Grant Number	Reported on FSRs	Provided	Expenditures	Expenditures
	_		_	_
05-6100-2053	\$499,798	\$499,799	\$226,864	\$272,935
06-6100-2043	\$423,053	\$423,499	\$232,261	\$191,238
07-6100-2069	\$501,540	\$501,540	\$239,225	\$262,315
$08-6100-2056^7$	\$ 48,499	\$191,254	\$191,254	-

Although the Council's expenditures generally matched the total outlays reported, we could not determine whether each component of the award was matched as required. The staff informed us that there is no particular matching applied to each component. For example, the notice of award for Grant Number 07-6100-2069, stated that although the overall grant could be matched on a one-to-one basis, the Arts Education component of the grant, in the amount of \$12,000 was to be matched on a one-to-one basis separately from the other components. We were unable to identify matching expenditures charged specifically for the Arts Education component. Grant Number 08-6100-2056 also required the Arts Education component to be matched one-to-one separately. Grant Numbers 06-6100-2043 and 05-6100-2053 required a one-to-one match for each individual component.

The Council also did not provide adequate documentation to support the matching expenditures for Grant Number 06-6100-2043, which included an American Masterpiece component, in the amount of \$5,000. The Council provided award documents to support expenditures in the amount of \$10,000. The documentation indicated that \$5,000 was awarded from the NEA grant and \$5,000 from the Council. However, the expenditure listing only included \$5,000 of NEA funds expended. As a result of inadequate documentation to support the matching expenditures, we are questioning \$5,000 included in the total outlays reported.

We recommend that the Council provide additional documentation to support the above questioned costs. We also recommend the Council develop written policies and implement procedures to ensure that its accounting system identifies and tracks accurate and allowable matching expenditures by component.

Check Distribution

Award checks are returned to the Council's office for distribution to recipients. During our review, we found recipients' award checks made payable to the recipients in "c/o Arts Council." We were informed by the staff that in some cases it is more convenient for the recipients to pick up the check from the Council's office because a P.O. Box may not be available. Segregation of duties is a deterrent to fraud and as the initiator and approver of award payments; the Council should not obtain custody of the checks.

We recommend that the Council develop written policies and implement procedures to provide adequate controls over award payments.

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⁷ Final report not due at time of audit.

Spending and Approval Authority

We reviewed several approved applications for major awards which were unilaterally approved by the Executive Director. In another instance, a major award was approved by the Arts Coordinator. We were informed by the Council staff that, before our site visit, the majority of its Board of Directors terms had expired; therefore, the Executive Director had been granted unlimited spending authority. The Council's applications for grants require that major awards (over \$1,500) must be approved by the Department of Community and Culture Affairs Secretary and the Board of Directors. The Council could not produce documentary evidence supporting the spending authority of the Executive Director.

For Grant Number 06-6100-2043, we found an application that did not have the required approval from the Council's Board of Directors and review panel in the amount of \$4,429. Such approval is required by the Council's Grant Application Guide. As a result, we are questioning expenditures in the amount of \$4,429 charged to the grant.

We recommend that the Council maintain written documentation of spending authorities and if necessary, document any revisions to that authority. The documentation should include position of authority, expenditures limits and period of coverage. We also recommend that the Council provide additional documentation to support the above questioned costs.

Travel Policies

We found that Council staff traveling on official business, paid for by the grant, did not attend all planned activities. A former Council official confirmed that when traveling to the "mainland" the staff was often "jet lagged" and may not have attended portions of the meetings or training. While expenses for training and transportation, and related items incurred by employees on official business is allowable, it must also be necessary and reasonable for <u>proper and efficient</u> performance and administration of Federal awards.

We recommend that the Council develop written policies and implement procedures which will ensure the appropriate and allowable use of Federal funds for travel. The Council should also develop written policies and implement procedures to ensure and require that staff attend all portions of training, conferences, seminar, meetings, etc. paid for by Federal funds.

Grant Application Guide

The Council provided us with a copy of its Grant Application Guide (Application Guide). The Application Guide was not dated and we found that some of the staff was not familiar with it. We were also informed that the Council staff did not provide the Application Guide to applicants. The Application Guide contains information on instructions and requirements for completing grant applications and program guidelines.

We recommend the Council revise and date its Grant Application Guide to reflect changes in NEA and Federal grant guidelines. The Council should provide copies to subrecipients and ensure that all employees are properly informed of its content.

Debarment and Suspension

The Council did not have procedures in place to ensure that recipients were not <u>debarred or suspended</u> prior to the award of Federal funds⁸. OMB Circular 102, Subpart C Section 35 states in part:

Federal awarding agencies and recipients shall comply with the nonprocurement debarment and suspension common rule implementing E.O.s 12549 and 12689, "Debarment and Suspension." This common rule restricts subawards and contracts with certain parties that are debarred, suspended or otherwise excluded from or ineligible for participation in Federal assistance programs or activities.

We recommend that the Council develop written policies and implement procedures to ensure that grants are not awarded to companies and or individuals which have been debarred or suspended from receiving Federal funds.

SECTION 504 SELF-EVALUATION

The Council did not have the required Section 504 self-evaluation on file. As noted in the *General Terms*, "A Section 504 self-evaluation <u>must</u> be on file at your organization." A *Section 504 Self-Evaluation Workbook* is available online at www.arts.gov/about/504Workbook.html.

Section 504 of the Rehabilitation Act of 1973, as amended, provides for equal opportunity to enter facilities and participate in programs and activities. It does not require that every part of every facility or program be accessible. The important considerations are that individuals with disabilities have the same opportunities in employment, the same opportunities to enter and move around in facilities, the same opportunities to communicate and the same opportunities to participate in programs and activities as non-disabled people. Further, it is important to offer employment, programs, and services in settings that are integrated rather than to segregate individuals with disabilities with special programs.

We recommended that the Council conduct a Section 504 self-evaluation to ensure compliance with the Rehabilitation Act of 1973, as amended. (A copy of the self-evaluation will be provided to NEA's Office of Civil Rights/EEO.)

METHOD OF FUNDING

The Council has been on the Working Capital Advance (WCA) method of funding since April 1991. WCA requires matching expenditures to be incurred, paid and documented before reimbursement. Although the Council was required to submit a summary sheet listing expenditures, they were not required to submit supporting documentation or an expenditure

⁸ Information may be obtained on parties that are debarred or debarred from receiving Federal funds from the General Services Administration (GSA) Excluded Parties List System web site at: https://www.epls.gov.

listing from its financial system. As stated above, our review of grant files and the Council's documentation concluded that expenditure listings and reports were inaccurate as a result of unallowable and questioned costs, math errors, and duplicate payments.

OMB A-102, Subpart B Section 12 states in part:

If an applicant or recipient: (a) has a history of poor performance, (b) is not financially stable, (c) has a management system that does not meet the standards prescribed in this Circular, (d) has not conformed to the terms and conditions of a previous award, or (e) is not otherwise responsible, Federal awarding agencies may impose additional requirements as needed...

Based on the length of time the Council has been on the WCA method of funding without improvement, the Council's history of not conforming to OMB and NEA requirements, or its internal guidelines; and its inadequate financial management system, we recommend that NEA: (1) consider the Council a "high-risk" grant recipient in accordance with 45 C.F.R. § 1174.12, (2) deem the Council ineligible to apply for or receive NEA awards, and (3) terminate all funding, including any suspended awards, until such time as the Council has implemented corrective actions to address the findings of this report and provide NEA with evidence of improvements in its management of Federal grants. If, in the future, NEA reinstates the Council's eligibility to receive funding, we recommend that it place the Council on the Cost Reimbursement method of funding.

Under the Cost Reimbursement method of funding, the grantee will be required to finance its operations with its own working capital with payments to be paid on a reimbursable basis for actual cash disbursements supported by adequate documentation. Costs are only reimbursed when required matching costs have also been incurred. *Documentation, generally, will take the form of an invoice, receipt or contract supported by a copy of a cancelled check/electronic copy or other document supporting that the transaction was enacted; e.g., bank statement, electronic reference, etc.* Specific documentation requirements will be established by the NEA Grants and Contracts Office.

EXIT CONFERENCE

An exit conference was held with the Council's staff on September 4, 2009. A telephone conference was also held with Council officials on August 16, 2010. They acknowledged and generally agreed with the findings and recommendations made to the Council, and indicated they were in agreement on implementing the recommendations.

RECOMMENDATIONS

We recommend the Council *develop written* policies and *implement* procedures to ensure:

- 1. Code of conduct and conflict of interest standards be established in accordance with the CNMI's *Department of Finance Division of Procurement and Supply CNMI Procurement Regulations, and* NEA *General Term*; and consistent with *OMB Circular A-102*.
- 2. The accounting system accurately identify and track only accurate and allowable expenditures charged as matching expenditures by specific award component.
- 3. Only actual and allowable costs are reported on its Requests for Advance or Reimbursement (payment requests) and final Federal Financial Report (FFR). Those procedures should also ensure:
 - a. Employees, who prepare the payment requests and FFRs, are familiar with the cost principles of OMB Circulars A-102 and A-87.
 - b. All reports and payment requests should be prepared in accordance with instructions from the NEA Grants and Contracts Office
 - c. An independent review of reports/payment requests is performed prior to submission to the NEA.
- 4. Capital equipment, purchased with Federal funding, is included in its project budget and pre-approved by NEA prior to purchase.
- 5. Personnel activity (time and effort) reports are maintained for any employee whose salary is charged, in whole or in part to future grant awards that are \$50,000 or more.
- 6. Only allowable travel expenses are charged to the grant and matching expenditures for eligible individuals in accordance with OMB Circular A-87.
- 7. All NEA grant funds are committed/obligated before the end of the award period as required.
- 8. Subrecipients are monitored in accordance with OMB Circular A-133 and all subrecipients' documentation is complete and maintained for a period of three years from the date of the Council's Final Financial Report submission to the NEA.
- 9. A written manual/handbook is developed containing policies and procedures relating specifically to managing Federal grants.

- 10. The Grant Application Guide is updated to reflect changes in NEA and Federal guidelines. The Council should provide copies to subrecipients and ensure that all employees become familiar with the Grant Application Guide.
- 11. Internal controls are strengthened by developing written policies and implementing procedures to provide adequate control over:
 - o all assets acquired with Federal funds,
 - o travel for staff,
 - o spending authority, and
 - o distribution of award payments.
- 12. Grants are not awarded to companies and or individuals that have been debarred or suspended from receiving Federal funds.
- 13. A Section 504 self-evaluation is conducted to ensure compliance with the Rehabilitation Act of 1973, as amended.
- 14. The Council submits additional documentation to the OIG to support questioned costs and/or other <u>allowable</u> costs charged to Grant Numbers 05-6100-2053, 06-6100-2043 and 07-6100-2069 matching expenditures. Without additional documentation a potential refund in the amount of \$337,666, may be due to the NEA (For details see Appendices B and C).

We also recommend that NEA:

- 15. Disallow the unallowable costs charged to the grants in the amount of \$141,049, reducing the total outlays reported by the indicated amounts for each grant (For details see Appendices B and C).
- 16. Consider the Council a "high-risk" grant recipient in accordance with 45 C.F.R. § 1174.12, (2) deem the Council ineligible to apply for or receive NEA awards.
- 17. Terminate all funding, including any suspended awards, until such time as the Council (1) has implemented corrective actions to address the findings of this report, (2) provide NEA with evidence of improvements in its management of Federal grants, and (3) NEA reinstates the Council's eligibility to apply for and receive awards.
- 18. Consider placing the Council on the Cost Reimbursement method of funding (as directed by the Grants and Contracts Office); if, in the future, NEA reinstates the Council's eligibility to apply for and receive awards.

COMMONWEALTH COUNCIL FOR ARTS AND CULTURE

SCHEDULE OF GRANTS SELECTED FOR AUDIT

Original Grant <u>Amount</u>	Grant Number	Grant Period	Reported <u>Costs</u>	Project Description
\$226,865*	05-6100-2053	10/01/05 - 09/30/07	\$ 499,798	To support partnership agreement activities.
\$234,755*	06-6100-2043	10/01/06 - 12/31/07	\$ 423,053	To support partnership agreement activities.
\$242,100*	07-61002069	10/10/07- 12/31/08	\$ 501,540	To support partnership agreement activities.
\$283,300**	08-6100-2056	10/01/08 - 09/30/09	\$ 48,499	To support partnership agreement activities.
\$ 25,000***	09-6188-2128	10/01/09 - 09/30/10	<u>\$</u> 0	To preserve or create jobs in the non-profit arts sector (ARRA).
\$1,012,020			<u>\$1,472,890</u>	

^{*} The final reports for these grants were submitted after the required 90-day deadline.

^{**} The final report for this grant was not due until September 9, 2009, subsequent to our review.

^{* * *} This grant was not selected for audit since no costs were reported.

COMMONWEALTH COUNCIL FOR ARTS AND CULTURE

Schedule of Disallowed/Questioned Costs and Potential Refunds – Direct Grants Reviewed

Grant Number	Original Grant <u>Amount</u>	Adjusted Grant Amount	Expenditure Amount <u>Reported*</u>	Total Documented <u>Costs Provided</u>	Less Disallowed <u>Costs⁹</u>	Less Questioned <u>Costs</u>	Potential <u>Refund¹⁰</u>
05-6100-2053	\$226,865	\$ 226,86211	\$499,798	\$499.799	\$37.070	\$207,547	\$99,271
06-6100-2043	\$234,755	231,815 ¹²	. ,	1 1 1	43.514	158.837	121.241
06-6100-2043	\$234,733	,	423,053	423,499	43,514	158,857	121,241
07-6100-2069	\$242,100	$237,724^{13}$	501,540	501,540	34,370	226,030	117,154
08-6100-2056	283,300	$283,300^{14}$	48,499	191,254	26,095	70,473	- 0-
Totals	<u>\$987,020**</u>	<u>\$979,701</u>	<u>\$1,472,890</u>	<u>\$ 1,616,092</u>	<u>\$141,049</u>	<u>\$675,332</u>	<u>\$337,666</u>

^{*}Per Final Financial Status Report or latest Request for Advance or Reimbursement at the time of site visit.

^{**} This total does not include Grant Number 09-6188-2128, in the amount of \$25,000.

Disallowed expenses charged to the grant according to relevant OMB Circulars A-87, A-102 and NEA *General Terms*.
Calculated as one-half of adjusted NEA grant amount plus matching requirement minus questioned/disallowed costs.
Original award less de-obligation in the amount of \$3.00.

Original award less de-obligation in the amount of \$3.00.

12 Original award less de-obligation in the amount of \$2,940.

13 Original award less de-obligation in the amount of \$4,376.

14 The final FSR for 08-6100-2056 was not due until December 31, 2009; therefore, at the time of the site visit, no refund was due.

COMMONWEALTH COUNCIL FOR ARTS AND CULTURE UNALLOWABLE AND QUESTIONED COSTS DETAIL

	05-6100-2053	06-6100-2043	07-6100-2069	08-6100-2056
TOTAL REPORTED OUTLAYS	\$499,799	\$423,499	\$501,540	\$191,254
UNALLOWABLE COSTS				
Mismanagement	\$11,250	\$7,100		
Conflict of Interest	\$20,700	\$23,801	\$16,675	\$3,200
Capital Equipment			\$17,695	\$22,895
Food and Entertainment	<u>\$5,120</u>	\$12,613	<u>-0-</u>	<u>-0-</u>
Less: Unallowable Costs	\$37,070	\$43,514	\$34,370	\$26,095
Subtotal: Allowable Cost	\$462,729	\$379,985	<u>\$467,170</u>	<u>\$165,159</u>
QUESTIONED COSTS				
Salaries and Wages	\$205,051	\$149,408	\$179,855	\$40,393
Travel Expenses	\$2,496	-0-	\$46,175	\$30,080
Matching Expenditures	-0-	\$5,000	-0-	-0-
Approval Authority	<u>-0-</u>	<u>\$4,429</u>	<u>-0-</u>	<u>-0-</u>
Less: Questioned Costs	\$207,547	\$158,837	\$226,030	\$70,473
Subtotal: Allowable Costs	<u>\$255,182</u>	<u>\$221,148</u>	<u>\$241,140</u>	<u>\$94,686</u>
Less: NEA Share of Allowable Costs	\$127,591	\$110,574	\$120,570	\$47,343
Adjusted Grant Amount	\$226,862	<u>\$231,815</u>	\$237,724	<u>-0-</u>
Potential Refund	<u>\$99,271</u>	<u>\$121,241</u>	<u>\$117,154</u>	<u>\$0</u>